ANNUAL REPORT 2005

DIAMOND TREE
ENERGY LTD.

Growth through the drill bit

Diamond Tree Energy is a Calgary-based company active in the exploration, development, and production of oil and gas in Western Canada. The Company has a proven management team with experience growing junior oil and gas companies in the Western Canadian Sedimentary Basin. Diamond Tree trades on the Toronto Stock Exchange under the symbol DT.

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DIAMOND TREE
ENERGY LTD.

2005 HIGHLIGHTS

Financial (000s except per share amounts)	Twelve Months Ended December 31, 2005	Twelve Months Ended December 31, 2004
Petroleum & natural gas sales	$50,631	$18,119
Cash flow from continuing operations	29,093	8,646
per share - basic (weighted average)	$1.50	$0.53
per share - diluted (weighted average)	$1.36	$0.51
per boe ($/boe)	34.11	19.01
Field netback ($/boe)	37.53	21.96
Net earnings from continuing operations	9,625	2,878
per share - basic (weighted average)	$0.50	$0.18
per share – diluted (weighted average)	$0.45	$0.17
Common shares outstanding (000s)		
Weighted average – basic	19,400	16,168
Weighted average – diluted	21,395	16,828
Total outstanding	22,495	18,712
Operations		
Average daily production		
Crude oil & NGL (bbl/d)	933	345
Natural gas (mcf/d)	8,423	5,406
Oil equivalent (boe/d)	2,337	1,246
Average product prices		
Crude oil & NGL ($/bbl)	$63.36	$43.57
Natural gas ($/mcf)	$9.45	$6.40
Undeveloped land ($000) -based on acquisition cost	$9,448	$3,184

MESSAGE TO SHAREHOLDERS

Dear shareholders,

We are pleased to present our 2005 Annual Report, a detailed review of our first full year as a publicly traded company (TSX: DT).

Diamond Tree significantly expanded its production, reserves, cash flow and earnings in 2005, all goals we set for ourselves at the beginning of the year. In addition, we increased our land holdings and prospect inventory to allow for continued growth in 2006 and beyond. While increasing our average daily production by 87% to 2,337 barrels of oil equivalent per day (boe/d), we were successful in keeping our operating costs at a very competitive rate of $5.89/boe. Our current production is approximately 2,600 boe/d.

Our team has now been working together for more than a year and everyone has meshed very well. All our employees are commended for their contribution to the 2005 results. Their diligence and hard work are traits that will drive our success in future years.

Our plan is to continue to grow through the drill bit. We will focus on projects where we have high ownership interests and operatorship where possible. Striving to add long-life oil and gas reserves will still be our main focus. We believe some of the steps taken in the last months of 2005 will be reflected in the successes to be achieved in 2006.

Our company is in a strong financial position as we execute our 2006 program. We are excited by the opportunities on our Peace River Arch and northeast B.C. land holdings and anticipate reporting positive results later this year.

Shareholders will notice that this year's Annual Report looks different than the one we produced last year. Diamond Tree has decided to join a growing trend away from the traditional format. We have opted to control our costs by using alternatives such as corporate profiles, press releases and the website to communicate our results and plans throughout the year.

Thank you to our Directors for their support and stewardship as the company grows and develops. A particular thanks to Mr. Fred Moore for his commitment and support since the start of Diamond Tree. Mr. Moore has decided not to put forward his name at the upcoming Annual General Meeting, thus allowing for the nomination of a completely independent Director. This decision greatly assists Diamond Tree in achieving the goal of nominating a slate of directors that will, if elected, form a board consisting of a majority of independent members.

While we prepare to say farewell to Mr. Moore, we are pleased to announce that Mr. John Mitchell has agreed to accept a nomination to the Board. Mr. Mitchell's name will be included on the slate of Directors proposed by the Governance Committee at the AGM.

We thank all of our shareholders for their continued support.

Don D. Copeland
Chairman & Chief Executive Officer

Kelly J. Ogle
President

MANAGEMENT'S DISCUSSION & ANALYSIS

March 10, 2006

This Management's Discussion and Analysis ("MD&A") for Diamond Tree Energy Ltd. (the "Company") should be read in conjunction with the audited consolidated financial statements and accompanying notes for the year ended December 31, 2005 in the annual report. The reporting currency, unless otherwise indicated, is Canadian dollars. Additional information relating to the Company, including the Company's Annual Information Form ("AIF") is available on SEDAR at www.sedar.com.

Statements throughout this MD&A that are not historical facts may be considered "forward-looking statements". These forward-looking statements sometimes include words to the effect that management believes or expects a stated condition or result. All estimates and statements that describe the Company's objectives, goals or future plans are forward-looking statements. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties and actual results could differ materially from those currently anticipated. These risks and uncertainties include, but are not limited to, volatility of oil and gas prices, commodity supply and demand, fluctuations in currency and interest rates, inherent risks associated in the exploration and development of oil and gas properties, ultimate recoverability of reserves, timing, results and costs of drilling activities and pipeline construction, availability of financing, new regulations and legislation, reinstatement of the Maximum Rate Limitation and availability of capital. Additional risks and uncertainties affecting the Company are contained in the Company's AIF. Forward-looking statements are based on current expectations, estimates and projections of future production and capital spending as at the date of this MD&A and the Company assumes no obligation to update or revise forward-looking statements to reflect new events or circumstances, except as required by law.

Per barrel of oil equivalent ("boe") amounts have been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil. BOE's may be misleading, particularly if used in isolation. The boe conversion ratio used is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

This MD&A contains the terms "cash flow from continuing operations", "cash flow from operations" and "field netback" which are non-GAAP financial measures that do not have any standardized meaning prescribed by Canadian Generally Accepted Accounting Principles ("GAAP") and are therefore unlikely to be comparable to similar measures presented by other issuers. Both "cash flow from operations" and "field netback" provide useful information to investors and management since they are an indicator of the Company's ability to fund future capital expenditures, which drives growth, and to repay debt. Cash flow from operations is calculated before changes in non-cash working capital. See "Non-GAAP financial measures" for a reconciliation of cash flow from operations and field netback to net earnings, the most comparable measure calculated in accordance with GAAP. The financial data presented has been prepared in accordance with GAAP. The reporting and the measurement currency is the Canadian dollar unless otherwise indicated.

Overview:

The Company was formed on December 31, 2004 as a result of the reverse takeover by Diamond Tree Resources Limited ("DTRL") of Wise Wood Corporation ("Wise Wood"). For accounting purposes, DTRL was deemed to have acquired Wise Wood and subsequent to the reverse takeover, Wise Wood changed its name to Diamond Tree Energy Ltd. Pursuant to a take over bid circular, Wise Wood acquired all the issued and outstanding shares of DTRL in exchange for four common shares of Wise Wood for each common share of DTRL. The shares of the Company were then consolidated on a 10 for 1 basis.
DTRL was a private company engaged in the business of oil and gas exploration and development while Wise Wood was a TSX Venture Exchange listed public company in the oil field services business. In May 2005, the Company sold its remaining oil field service business assets to an arms length party.

All comparative figures are those of DTRL. Any disclosure of share, option or per share data in the financial statements reflects the post merger share structure.

Consolidated Financial Results:

For the year ended December 31,		2005		2004
Revenue, net of royalties	$	**37,036,022**	$	14,233,252
Cash flow from continuing operations	$	**29,092,830**	$	8,646,137
-per common share – diluted	$	**1.36**	$	0.51
Net earnings from continuing operations	$	**9,625,417**	$	2,877,740
-per common share – diluted	$	**0.45**	$	0.17

Cash flow from continuing operations of $29.1 million ($1.36 per diluted common share) increased 236% from 2004 levels due to higher sales volumes and stronger field netbacks. Higher field netbacks were driven by strong commodity prices and lower per unit operating costs.

2005 net earnings from continuing operations were $9.6 million ($0.45 per diluted common share), up from $2.9 million ($0.17 per diluted common share) in 2004. Stronger 2005 earnings were due to higher cash flow being only partially offset by higher interest, depletion, stock based compensation and future tax expense.

Acquisitions, Dispositions and Discontinued Operations:

On November 17, 2004, DTRL closed the corporate acquisition of Edenshaw Resources Ltd. ("Edenshaw"), a private oil and gas company, for aggregate cash consideration of $5.6 million. The assets of Edenshaw consisted of working interests in lands and wells in the Ferrybank area of Alberta where DTRL already held the majority working interest and acted as operator. As a result of this acquisition, the Company increased its working interests in one of its core areas, Ferrybank, from 80% to 100%.

On December 31, 2004, DTRL closed the corporate acquisition of Wise Wood, at a deemed cost of $2.4 million ($0.175 per common share). This acquisition was effectively a "going public" transaction for DTRL and the combined Company began trading on the TSX Venture Exchange as Diamond Tree Energy on January 11, 2005. In April 2005, the Company graduated to the TSX. DTRL had been a private company engaged in the business of oil and gas exploration and development while Wise Wood was a TSX Venture Exchange listed public company in the oil field services business. After the merger, the Company adopted a plan to divest of Wise Wood's oil field services business. As a result, assets, liabilities, income and expenses related to the oilfield service business have been included in the 2005 financial statements as discontinued operations.

On May 2, 2005 the Company sold its oil field service assets to Eveready Income Fund, a publicly traded entity, for total proceeds of $4.65 million. Proceeds partly consisted of 1.2 million trust units of Eveready Income Fund, which were valued at $3.75 per unit. The Company recognized a $2.5 million loss upon disposal of the oilfield service assets but this was reduced by the $2.0 million gain on the ultimate sale of the trust units. For 2005, the overall loss from discontinued operations, including revenue and expenses from the oil field service business prior to its disposition, was $0.4 million. During 2005, the bank loan, U.S. dollar denominated notes and the secured, convertible debentures were paid in full using the proceeds from divesting of the oilfield service assets. At year end, the only balance sheet item related to discontinued operations was accounts receivable of $0.4 million, which was collected subsequent to year end.

Effective June 30, 2005 and closing September 30, 2005, the Company sold its minor heavy oil interests in Saskatchewan to a private oil and gas company for cash proceeds, net of adjustments, of $296,000.

Results of Operations:

Petroleum and natural gas sales – variance analysis:

		Change due to:		
($000's)	**2005**	Pricing	Volume	2004
Natural gas sales	**$29,050**	$9,371	$7,043	$12,636
Crude oil and natural gas liquids sales	**21,581**	6,743	9,355	5,483
Total petroleum and natural gas sales	**$50,631**	$16,114	$16,398	$18,119

Petroleum and natural gas sales for the year ended December 31, 2005 were $50.6 million, $32.5 million above 2004 levels. This positive variance can be attributed equally to stronger commodity prices and higher sales volumes resulting from drilling successes.

Natural gas sales:

	2005	2004	% Change
Natural gas price ($/mcf)	**$9.45**	$6.40	48
Natural gas production (mcf/d)	**8,423**	5,406	56

Crude oil and natural gas liquids sales:

	2005	2004	% Change
Crude oil and natural gas liquids price ($/bbl)	**$63.36**	$43.57	45
Crude oil and natural gas liquids production (bbl/d)	**933**	345	170

Natural gas volumes grew by 56% to average 8,423 mcf/d while oil volumes increased 170% to average 933 bbl/d for the year. During 2005 the Company drilled 25 (23.1 net) wells, resulting in 16 gas wells, six oil wells and three abandoned wells. Of the 16 gas wells, 10 were on-stream prior to the end of 2005 or early in 2006. Of the six oil wells, four were on-stream prior to the end of 2005 or early in 2006.

In Alberta, AECO gas prices averaged $8.69/mcf (CDN) in 2005, up 32% from 2004 due primarily to stronger North American demand. The Company's 48% increase in its realized gas price exceeded the benchmark due to the relatively higher heating content of its natural gas. The benchmark crude oil price for West Texas Intermediate at Cushing Oklahoma increased 37% from 2004 to average $56.61/bbl (USD) while crude oil prices at Edmonton City Gate increased 31% to $68.99/bbl (CDN). These price increases were due mainly to production woes associated with hurricane activity in the Gulf Coast region as well as ongoing geo-political uncertainty in oil producing regions overseas. 2005 The Company saw a 45% increase in its realized oil and natural gas liquids price, consistent with the benchmark trends.

Royalties, net of ARTC:

	2005		2004	
	$000's	**Rate %**	$000's	Rate %
Natural gas	**$8,147**	**28**	$3,053	24
Crude oil and natural gas liquids	**5,929**	**27**	1,303	24
Alberta royalty tax credit (ARTC)	**(481)**		(470)	
Total royalties, net of ARTC	**$13,595**	**27**	$3,886	21

Royalty rates generally increase as commodity prices increase. During the second half of 2005, Diamond Tree exceeded the threshold for ARTC purposes, causing the effective royalty rate for Crown royalties in excess of $2.0 million to increase. Diamond Tree also pays gross overriding and freehold royalties, primarily on its production at Ferrybank, which causes the effective royalty rate to rise. It is anticipated that production from the Company's new areas will come primarily from Crown lands.

Operating expenses:

	2005		2004	
	$000's	**$/boe**	$000's	$/boe
Operating expenses	**5,026**	**5.89**	4,246	9.34

2005 per-unit operating costs have trended downward from 2004 as fixed operating charges were spread across a larger production base, lower-cost production was brought on-stream and operational efficiencies were realized. Year to date operating costs of $5.89/boe are significantly below previous 2005 full year operating cost guidance of $7.00/boe. 2005 operating expenses include $417,000 of transportation costs.

Field netback:

	2005		2004	
	$000's	**$/boe**	$000's	$/boe
Petroleum and natural gas sales	**$50,631**	**$59.36**	$18,119	$39.85
Royalties, net of ARTC	**(13,595)**	**(15.94)**	(3,886)	(8.55)
Other income	**---**	**---**	2	---
Operating expenses	**(5,026)**	**(5.89)**	(4,246)	(9.34)
Field netback	**$32,010**	**$37.53**	$9,989	$21.96
Volumes (boe/d)		**2,337**		1,246

Field netbacks increased on both a total basis and per-unit basis for the year ended December 31, 2005 due to increased volumes, higher realized commodity prices and lower per-unit operating costs.

General and administrative expenses:

	2005			2004		
	$000's	**%**	**$/boe**	$000's	%	$/boe
Total	**$2,972**			$1,867		
Recoveries	**(127)**			(60)		
Capitalized	**(695)**	**24%**		(712)	38%	
Net expensed	**2,150**	**76%**	**2.52**	1,095	62%	2.41
		100%			100%	

Diamond Tree's increased activity, administration of a larger capital program and expenditures associated with graduating to the Toronto Stock Exchange generated higher general and administrative expenses but due to a significant year over year increase in production volumes, expenses on a per-unit basis saw only a modest increase.

Interest expense:

Interest expense of $510,000 is comprised of interest on bank loans and interest associated with a capital lease relating to field infrastructure. During the fourth quarter of 2005, interest on bank loans was minimal as a result of the private placement in late September 2005. At the end of 2005, the Company had no amounts drawn against its $24.0 million bank loan, allowing it to use bank borrowings, combined with cash flow from operations, to fund its 2006 capital program.

Depletion, amortization and accretion:

	2005		2004	
	$000's	**$/boe**	$000's	$/boe
Oil and gas	**$12,126**	**$14.21**	$4,326	$9.52
Office furniture and equipment	**14**	**0.02**	6	0.01
Accretion	**101**	**0.12**	50	0.11
Total provision	**$12,241**	**$14.35**	$4,382	$9.64

The depletion, amortization and accretion provision for the year ended December 31, 2005 was $12.2 million, $7.8 million higher than 2004 due to increased production volumes and per-unit depletion rates. Diamond Tree spent approximately $17.6 million on capital expenditures in the fourth quarter and some of the drilling results are not yet reflected in the estimate of total reserves due to ongoing evaluations of new wells. In subsequent quarters, capital expenditures incurred in the fourth quarter may be allocated additional reserves. The fourth quarter depletion rate was also affected by the province-wide rescission of the Maximum Rate Limitation, which is further discussed in the section entitled "Summary of Quarterly Results". The Company's external evaluation engineers have provided year end reserve numbers for 2005.

Taxes:

Diamond Tree's tax horizon depends on factors such as production levels, commodity prices, tax classifications of wells drilled and the nature of capital expenditures throughout the year. Although the Company spent $43.5 million on capital during the year and $17.3 million in the fourth quarter, higher production, strong commodity prices and low operating costs created taxable income in the fourth quarter of 2005. Current income tax expense, including capital taxes, is estimated to be approximately $0.2 million. A summary of estimated tax pools at December 31, 2005 as well as reconciliation between the expected tax rate and the actual tax rate is provided in Note 8 of the audited consolidated financial statements.

Use of proceeds of private placement:

On September 29, 2005, Diamond Tree closed a private placement of 3.5 million common shares at $5.10 per share for approximate net proceeds of $16.8 million. Proceeds from the private placement were to be used to facilitate the expansion and acceleration of the Company's operations through acquisition, exploration and development drilling. The following table shows the use of proceeds.

	$ millions
Proceeds, net of share issue costs	$16.8
Extinguish outstanding bank loan	(12.4)
Partially fund fourth quarter capital of $17.3 million	(4.4)

Repayment of outstanding bank debt will allow the Company to use bank borrowings, combined with cash flow from operations, to fund its 2006 capital program.

Liquidity and Capital Resources:

Cash flow:

The Company believes that its existing credit facilities and expected cash flow from operations will be sufficient to fund its planned capital investment program and enable it to meet all current and expected financial requirements. Other than the items noted in the "Commitments" section of this MD&A, capital spending is discretionary. Refer to the "Outlook" section for a discussion of the Company's future plans.

Cash flow from continuing operations for 2005 was $29.1 million or $1.36 per diluted share. This compares favorably to $8.6 million or $0.51 per diluted share in 2004. This 236% increase from 2004 is due to higher sales volumes and stronger field netbacks. Higher field netbacks were driven by strong commodity prices and lower per unit operating costs.

The following table summarizes cash flow from continuing operations per unit of production:

	2005		2004	
-	**$000's**	**$/boe**	$000's	$/boe
Field netback	**$32,010**	**$37.53**	$9,989	$21.96
General and administrative expenses (1)	**(2,229)**	**(2.61)**	(1,094)	(2.41)
Interest expense	**(510)**	**(0.60)**	(245)	(0.53)
Current taxes	**(178)**	**(0.21)**	(4)	(0.01)
Cash flow from continuing operations	**$29,093**	**$34.11**	$8,646	$19.01

(1) 2005 G&A includes stock based compensation of $79,000.

Bank loan:

At December 31, 2005 the Company had no bank debt, a $24.0 million revolving operating loan facility available with a Canadian chartered bank and cash on hand. At the end of the third quarter, net proceeds from the private placement were applied to pay off the outstanding loan balance. Drawings on the loan facility bear interest at the bank's prime rate plus 0.25%. The next annual review date has been scheduled for April 30, 2006 at which time the externally prepared reserve report effective December 31, 2005 will determine the basis for any changes to this facility. Security for this facility is by way of a general security agreement providing a security interest over all present and after acquired personal property and a floating charge on all lands. At December 31, 2005 there were no covenant violations.

Working capital:

At December 31, 2005, the Company had a working capital deficit of $5.8 million primarily due to its busy fourth quarter capital program. The combination of un-drawn credit facilities and cash on hand is sufficient to cover this working capital deficit.

Equity:

During 2005, the Company raised net proceeds of $16.8 million through private placements. On September 29, 2005, the Company closed a private placement resulting in the issuance of 3.5 million common shares at $5.10 per share of which 22,000 shares were issued to directors, officers and employees. On November 10, 2005, the Company closed a private placement to an employee resulting in the issuance of 9,400 common shares at $5.35 per share. During 2005, option exercises provided cash of $358,000.

At December 31, 2005 the Company had 22,495,198 common shares issued and outstanding. At March 10, 2006, the Company had 22,608,198 common shares, 2,173,000 options and 2,500,000 performance warrants outstanding.

Capital expenditures:

Exploration and development spending during the 2005 is as follows:

$ millions	**Full Year 2005**	Oct-Dec 2005	Jul-Sep 2005	Apr - Jun 2005	Jan - Mar 2005
Land and property acquisitions	**7.3**	1.8	2.5	1.1	1.9
Dispositions	**(0.3)**	0.0	(0.3)	0.0	0.0
Seismic and geological and geophysical	**0.8**	0.5	0.1	0.1	0.1
Intangible drilling, completions and re-completions	**27.3**	12.7	10.1	4.1	0.4
Well equipment and facilities	**6.5**	1.9	1.4	1.4	1.8
Capitalized general and administrative expense	**0.7**	0.4	0.1	0.1	0.1
Capital expenditures before capital lease	**42.3**	17.3	13.9	6.8	4.3
Capital lease for field compression	**1.2**	-	-	-	1.2
Capital expenditures after capital lease	**43.5**	17.3	13.9	6.8	5.5

Drilling, completion and tie-in activity accounted for 80% of yearly capital expenditures. During 2005 the Company drilled 25 (23.1 net) wells, resulting in 16 gas wells, six oil wells and three abandoned wells. Of the 16 gas wells drilled, 10 were on-stream prior to year end or early in 2006. Of the six oil wells drilled, four were on-stream prior to year end or early in 2006. Other capital spending activity was focused on completing tie-in operations for the wells drilled at the end of 2004 and installing infrastructure to de-bottleneck production.

During 2005, the Company acquired 22,400 acres through land sales in both its west central core area as well as new areas further west of the fifth meridian. The Company announced two farm-ins in 2005 -- one in the Peace River Arch area of Alberta on July 25 and one in the Tupper/Cutbank area of northeast B.C. on December 12. Diamond Tree continues to acquire landholdings on prospects in various stages of development to add to its 2006 drilling schedule. The Peace River Arch area has seen increased activity, resulting in a competitive environment for land and services in this prolific area.

Goodwill:

At December 31, 2005 the Company had goodwill of $246,515 recorded on its consolidated balance sheet as a result of the acquisition of Edenshaw. Refer to the "Acquisitions and Dispositions" section of this MD&A. Goodwill is not amortized but tested for impairment at least on an annual basis, at which time any identified impairment would be charged to income. At December 31, 2005, there was no impairment related to goodwill.

Commitments:

At December 31, 2005 the Company has committed to future payments as follows:

	Total	**Less than 1 year**	**1 – 3 years**	**After 3 years**
Operating leases (CDN$) – note (i)	253,250	253,250	---	---
Capital lease obligations – note (ii)	981,669	267,248	714,421	---
Farm-in commitment (CDN$) – note (iii)	4,500,000	4,500,000	---	---
Total contractual obligations	5,734,919	5,020,498	714,421	---

(i) This is comprised of office and equipment leases.

(ii) This is a lease for field compression facilities which is a capital lease for accounting purposes.

(iii) On December 12, 2005, the Company announced the signing of a farm-in agreement with a four well commitment. On February 3, 2006, the Company entered into an agreement to acquire additional seismic data over the farm-in area. Estimated committed drilling and seismic costs relating to this farm-in over the next twelve months total $4.5 million.

Critical Accounting Estimates:

The preparation of financial statements that conform with Canadian GAAP requires management to make the following estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and revenues and expenses for the period then ended.

Full Cost Accounting – The Company follows the full cost method of accounting. All costs for exploration and development of reserves are capitalized in a country by country cost centre; the costs are then depleted on the unit of production method based on estimated proved reserves. The estimation of reserves is subject to a number of risks and uncertainties as described below. The capitalized costs can not exceed a ceiling amount. If the capitalized costs are determined to be in excess of this reserve-based ceiling amount, the excess is written off. The financial statement line items affected by this accounting estimate are property and equipment on the balance sheet (through the provision for accumulated depletion and amortization) and depletion, amortization and accretion on the income statement. Accordingly, changes to this accounting estimate can have a significant impact on total assets and net income but no direct cash flow impact. In

compliance with accounting standards, the reserve-based ceiling amount is an estimate that is revisited, and possibly adjusted, at each balance sheet date, to coincide with changes to the latest reserve estimate. An alternative method of accounting for oil and natural gas operations is the successful efforts method. Under this method the cost centre is defined to be a property rather than a country cost centre and exploratory dry holes and geological and geophysical costs are charged to earnings when incurred.

Reserves – The Company engages independent qualified reserve evaluators to evaluate its reserves each year. Reserve determinations involve forecasts based on property performance, future prices, future production and costs, and the timing of expenditures; all these are subject to uncertainty. The financial statement line items affected by this accounting estimate are property and equipment on the balance sheet (through the provision for accumulated depletion and amortization) and depletion, amortization and accretion on the income statement. Accordingly, changes to this accounting estimate can have a significant impact on total assets and net income but no direct cash flow impact. Reserves at the end of each year are based on a report obtained from qualified reserve evaluators. This estimate of reserves will change from one year to the next, thus causing changes in current year amounts booked to the balance sheet and income statement. Reserve revisions can change reported depletion and depreciation and earnings; downward revisions could result in a ceiling test writedown. Refer to the Company's AIF to see a reconciliation of the year over year changes in reserves.

Asset Retirement Obligation – The Company provides for the estimated abandonment costs using a fair value method based on cost estimates determined under current legislative requirements and industry practice. The amount of the liability is affected by the estimated cost per well, the timing of the expenditures and the discount factor used. The financial statement line items affected by this accounting estimate are property and equipment on the balance sheet (through the inclusion of an asset retirement cost), asset retirement obligation on the balance sheet and depletion, amortization and accretion on the income statement. Accordingly, changes to this accounting estimate can have a significant impact on total assets, total liabilities and net income but no direct cash flow impact. Total future asset retirement obligations are estimated by management based on the Company's working interest in its wells and facilities, estimated costs to remediate, reclaim and abandon the wells and facilities, before deduction of salvage values, and the estimated timing of the costs to be incurred in future periods. To assist in estimating salvage values and timing of abandonment costs, management uses the estimates and assumptions found in the reserve report obtained from qualified reserve evaluators. This reserve report will change from one year to the next, thus causing changes in current year amounts booked to the balance sheet and income statement.

Stock based Compensation – The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which were fully tradable with no vesting restrictions. This option valuation model requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options and performance incentive warrants have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the calculated fair value, such value is subject to measurement uncertainty. The financial statement line items affected by this accounting estimate are contributed surplus on the balance sheet and stock based compensation on the income statement. Accordingly, changes to this accounting estimate can have a significant impact on shareholders equity and net income but no direct cash flow impact. Assumptions used in the Black – Scholes option pricing model such as stock volatility, interest rates and expected life of the option change based on trading behavior of the Company's stock as well as overall economic conditions. Increased stock volatility results in higher compensation cost for new stock issuances, leading to lower net income.

Risk Management:

Crude oil and natural gas operations involve certain risks and uncertainties. These risks include, but are not limited to, operational, safety and environmental, credit, interest rate, foreign exchange rate and commodity price risk. For a more detailed description of the risks and uncertainties faced by the Company, refer to the Company's AIF.

Operational risks are managed through engaging competent field personnel and a comprehensive insurance program designed to protect the Company from significant losses arising from risk exposures.

Safety and environmental risks are addressed by compliance, in all material respects, with government regulations as well as adoption and compliance of the Company's safety and environmental standards policy.

Substantially all the Company's accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks with such exposure being within acceptable levels. At December 31, 2005, 82% (2004 – 74%) of the Company's accounts receivable were from one customer and related to one month of production revenue.

The Company is exposed to fluctuations in interest rates with respect to its bank borrowings but as at December 31, 2005 had no amounts borrowed against such facilities.

The Company is exposed to foreign-currency fluctuations as crude oil and natural gas prices received are referenced to U.S. dollar denominated prices.

Risks associated with commodity prices, interest and exchange rates are generally beyond the control of the Company; however, various hedging products may be considered to reduce the volatility in these areas. The Company has no hedging contracts or fixed-price physical contracts in place at this time.

Summary of Quarterly Results:

The following table highlights the Company's quarter over quarter growth. Financial data has been prepared in accordance with GAAP and amounts shown are in Canadian dollars. Information for quarters prior to September 30, 2004 is not available since DTRL was not a reporting issuer during 2004 and did not prepare quarterly financial information.

($000s except per share and boe amounts)	2005 Q4	2005 Q3	2005 Q2	2005 Q1	2004 Q4	2004 Q3
Production (boe/d)	**2,992**	2,565	1,859	1,917	1,366	1,077
Revenue	**19,153**	15,057	8,384	8,036	5,412	4,044
Revenue ($/boe)	**69.58**	63.82	49.55	46.57	43.06	40.82
Cash flow from continuing operations	**11,083**	8,992	5,056	3,962	2,684	1,627
Cash flow from continuing operations - per share basic	**$0.53**	$0.48	$0.28	$0.21	$0.16	$0.10
Cash flow from continuing operations - per share diluted	**$0.47**	$0.44	$0.25	$0.20	$0.15	$0.10
Net earnings from continuing operations	**3,352**	3,540	1,756	977	611	295
Net earnings (loss)	**5,549**	3,522	1,385	(1,204)	611	295
Net earnings from continuing operations – per share basic / diluted	**$0.16 $0.14**	$0.19 $0.17	$0.10 $0.09	$0.05	$0.04	$0.02
Net earnings (loss) – per share basic / diluted	**$0.28 $0.25**	$0.19 $0.17	$0.07 $0.07	($0.06)	$0.04	$0.02

During the fourth quarter of 2005, production increased due to new wells being brought on stream as well as the relaxation of the Maximum Rate Limitation ("MRL") by the Alberta Energy and Utilities Board ("EUB"). For the last four months of 2005, the MRL had been rescinded province-wide in an effort to help alleviate North American production woes associated with hurricanes in the Gulf Coast. During this period, the MRL relaxation allowed Diamond Tree to produce its Niton field at an increased rate of approximately 1,400 boe/d. On January 1, 2006, the EUB reinstated the MRL and production from the Niton area has been restricted to approximately 385 boe/d. An application for Good Production Practice has been withdrawn by the Company, pending further development of the pool and waterflood studies.

Higher production combined with stronger commodity prices helped fourth quarter cash flow from continuing operations exceed third quarter levels by $2.1 million. In addition to quarter over quarter growth in production and stronger commodity prices, downward trending operating costs have also contributed to stronger cash flow from continuing operations.

Fourth quarter net income from continuing operations came in slightly lower than third quarter levels as strong fourth quarter cash flow was offset by higher non-cash stock based compensation and depletion and depreciation expense. Although accelerated production from the Niton field due to the rescission of the MRL served to increase the depletion rate, the non-cash cost of a higher depletion rate is more than offset by the benefit of generating higher production from this field during the fourth quarter when commodity prices were strong. Year end reserve numbers have been provided by the Company's external evaluation engineers with some drilling results not yet reflected in the estimate of total reserves due to ongoing evaluations of new wells. In subsequent quarters, capital expenditures incurred in the fourth quarter of 2005 may be allocated additional reserves.

Selected Annual Information:

The following financial data has been prepared in accordance with GAAP for each of the three most recently completed financial years. Amounts are in Canadian dollars.

Year ended December 31,	2005	2004	2003
(000's except per share amounts and production)			
Production – boe/d	**2,337**	1,246	656
Revenue	**$50,631**	$18,119	$8,841
Net earnings from continuing operations	**9,625**	2,878	842
per share - basic	**$0.50**	$0.18	$0.05
per share - diluted	**$0.45**	$0.17	$0.05
Net earnings	**9,251**	2,878	842
per share - basic	**$0.48**	$0.18	$0.05
per share - diluted	**$0.43**	$0.17	$0.05
Total assets	**75,142**	46,653	19,988
Total long-term liabilities	**14,608**	10,556	3,632
Shareholders' equity	**46,286**	17,557	9,604
Cash dividends declared	nil	nil	nil

Over the last three years, the Company's average daily production has grown primarily through increased drilling activity. Growth in production, combined with stronger year over year commodity prices, has led to higher revenue and net income. During 2005, the Company had discontinued operations relating to the December 31, 2004 reverse takeover of Wise Wood. These assets were disposed of on May 2 and the Company incurred a loss from discontinued operations of $0.4 million during 2005.

Outlook:

Certain information contained in this section constitutes "forward looking statements". Refer to the introduction of this MD&A. As outlined in its November 21, 2005 press release, Diamond Tree's Board of Directors has approved a $50 million capital expenditure budget for 2006, with $41 million directed towards drilling, completing and equipping activities and $9 million towards land and seismic acquisition. In part, the Company's 2006 capital program is designed to increase its inventory of undeveloped land. Diamond Tree expects to drill at least 30 net wells in 2006, consisting of five shallow wells, 15 medium wells and 10 deep wells. The Company anticipates funding 2006 budgeted capital expenditures through internally generated cash flow from operations and bank debt. These estimates do not include the effect of any property acquisitions that may occur.

Diamond Tree currently has two drilling rigs and one service rig operating in the field. To date in 2006, the Company has drilled and cased seven wells which are in various stages of completion. The Company expects to drill three more wells prior to spring break-up. Diamond Tree has experienced marked delays in the field as a result of weather or access to equipment and services, especially regarding the equipping and tie-in of wells drilled late in 2005 and early in 2006. Pipeline tie-ins and facility construction are underway in the Niton, Woodland, Garrington, Minnehik, Crossfield, Gold Creek and Karr areas. Production is expected to be in the 2,500 to 2,600 boe/d range in early April with an additional 750 boe/d of behind pipe production. Due to the above noted delays and the onset of the spring break-up period, Diamond Tree is reducing its previously disclosed guidance regarding 2006 average yearly production from 3,500 boe/d to 3,000 boe/d. 2006 guidance pertaining to estimated exit rate production of 4,500 boe/d, total capital spending and the number of wells expected to be drilled remains unchanged. Diamond Tree continues to acquire landholdings on prospects in various stages of development to add to its 2006 drilling schedule.

Sensitivities:

The Company's results and ability to generate sufficient amounts of cash to fund ongoing operations are affected by external market factors such as fluctuations in the prices of crude oil and natural gas as well as movements in foreign-exchange rates. Changes in production can also affect cash flow. Sensitivities to these factors are summarized below:

	2006 impact on ➔	Cash flow from continuing operations ($000's)	Cash flow from continuing operations / share[1]
Gas price	+ CDN $0.50/mcf	$1,278	$0.06
Oil price	+ USD $1.00/bbl	$223	$0.01
Gas prod	+1000 mcf/d	$1,240	$0.06
Oil prod	+100 bbls/d	$844	$0.04
Currency	+CDN $0.01	$102	$0.005

[1] Per share figures are based on 22,495,198 basic shares outstanding as at December 31, 2005.

Non-GAAP financial measures:

The following table reconciles the non-GAAP financial measures "cash flow from continuing operations", "cash flow from operations" and "field netback" to "net earnings from continuing operations", the most comparable measure calculated in accordance with GAAP:

	Q4/2005	Q3/2005	Q2/2005	Q1/2005	Q4 / 2004	Q3 / 2004
Net earnings from continuing operations	**$3,351,798**	$3,540,312	$1,756,117	$977,189	$610,986	$295,234
Add back items not involving cash:						
Depletion, amortization and accretion	**4,840,041**	3,078,807	2,082,584	2,239,935	1,361,045	1,249,752
Future income taxes	**1,584,877**	2,086,000	1,041,000	573,000	152,190	82,479
Stock based compensation	**1,306,481**	286,576	175,870	172,242	559,481	---
Cash flow from continuing operations	**$11,083,197**	$8,991,695	$5,055,571	$3,962,366	$2,683,702	$1,627,465
Cash flow from discontinued operations	**332,279**	(18,653)	(59,053)	(47,605)	---	---
Cash flow from operations	**$11,415,476**	$8,973,042	$4,996,518	$3,914,761	$2,683,702	$1,627,465
Add back items not directly related to field operations:						
Other income	**52,378**	(778)	(51,600)	---	---	---
Discontinued operations cash flow	**(332,279)**	18,653	59,053	47,605	---	---
General and administrative expense [1]	**908,698**	427,407	322,123	571,261	472,526	222,916
Interest	**52,550**	173,238	153,606	130,540	86,872	44,749
Current taxes	**153,700**	---	(23,550)	48,000	---	---
Field netback	**$12,250,523**	$9,591,562	$5,456,150	$4,712,167	$3,243,100	$1,895,130

[1] Q4/2005 figure includes stock based compensation expense of $79,000.

Conclusions regarding the effectiveness of disclosure controls and procedures:

Effective for the year end 2005, securities regulations state that the Company is to evaluate the effectiveness of its disclosure controls and procedures over financial reporting and disclose in its MD&A the conclusions of such evaluation.

Disclosure controls are procedures designed to ensure that information required to be disclosed in reports filed with securities regulatory authorities is recorded, processed, summarized and reported on a timely basis and is accumulated and communicated to the Company's management, including the CEO and CFO as appropriate, to allow timely decisions regarding required disclosure.

Based on the evaluation conducted, the CEO and CFO concluded that the design and operation of disclosure controls and procedures were effective as at December 31, 2005 to provide reasonable assurance that material information relating to the Company would be made known to them by others within the organization.

AUDITORS' REPORT

To the Shareholders of Diamond Tree Energy Ltd.

We have audited the consolidated balance sheets of Diamond Tree Energy Ltd. as at December 31, 2005 and the statements of income and retained earnings and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The comparative financial statements as and for the year end presented for the comparative purposes December 31, 2004 were audited by another firm of Chartered Accountants which expressed an opinion without reservation on those financial statements in their report dated March 2, 2005.

Deloitte & Touche LLP

Chartered Accountants
Calgary, Alberta
March 3, 2006

Consolidated Balance Sheets

As at December 31,		2005		2004
Assets				
Current assets:				
Cash and cash equivalents (note 2(n))	$	549,856	$	2,027,065
Accounts receivable		7,296,953		2,986,268
Prepaid expenses		131,907		137,295
Current assets of discontinued operations (note 15)		422,947		1,153,209
		8,401,663		6,303,837
Property and equipment (note 4)		66,493,915		33,756,420
Non-current assets of discontinued operations (note 15)		---		6,345,805
Goodwill (note 3)		246,515		246,515
	$	75,142,093	$	46,652,577
Liabilities and Shareholders' Equity				
Current liabilities:				
Accounts payable and accrued liabilities	$	13,827,238	$	6,317,676
Bank loans (note 5)		---		10,501,424
Income taxes payable (note 8)		153,700		91,459
Current portion of capital lease (note 6)		267,248		---
Current liabilities of discontinued operations (note 15)		---		1,629,161
		14,248,186		18,539,720
Non-current liabilities of discontinued operations (note 15)		---		3,000,000
Capital lease (note 6)		714,421		---
Asset retirement obligation (note 7)		2,393,797		956,059
Future income taxes (note 8)		11,500,000		6,600,000
Total liabilities		28,856,404		29,095,779
Shareholders' equity:				
Share capital (note 9(b))		32,091,707		14,545,470
Share purchase loan (note 10)		(650,000)		(650,000)
Contributed surplus (note 11)		2,491,106		559,481
Retained earnings		12,352,876		3,101,847
		46,285,689		17,556,798
Commitments and contingencies (note 12)				
Subsequent events (note 17)				
	$	75,142,093	$	46,652,577

See accompanying notes to the consolidated financial statements

Approved by the Board:

Don D. Copeland
Director

Howard Dixon
Director

Consolidated Statements of Income and Retained Earnings

For the year ended December 31,		2005		2004
Revenue:				
Petroleum and natural gas sales	$	50,631,167	$	18,119,240
Royalties, net of Alberta royalty credits		(13,595,145)		(3,885,988)
Other		---		1,955
		37,036,022		14,235,207
Expenses:				
Operating		5,025,619		4,245,777
General and administrative		2,150,448		1,094,809
Stock based compensation (notes 9 and 10)		2,020,169		559,481
Interest on bank loans (note 5)		443,610		244,513
Interest on capital lease (note 6)		54,182		---
Interest - other		12,142		---
Depletion, amortization and accretion		12,241,367		4,382,247
		21,947,578		10,526,827
Earnings from continuing operations before income taxes		15,088,444		3,708,380
Income taxes, continuing operations (note 8):				
Current		178,150		3,971
Future		5,284,877		826,669
		5,463,027		830,640
Net earnings from continuing operations		9,625,417		2,877,740
Loss from discontinued operations (note 15)		374,388		---
Net earnings		9,251,029		2,877,740
Retained earnings beginning of year		3,101,847		224,107
Retained earnings end of year	$	12,352,876	$	3,101,847
Net earnings from continuing operations				
Earnings per share – basic		$0.50		$0.18
-- diluted[1]		$0.45		$0.17
Loss from discontinued operations				
Per share -- basic and diluted		($0.02)		---
Net earnings				
Earnings per share – basic		$0.48		$0.18
-- diluted[1]		$0.43		$0.17
Weighted average shares outstanding				
Basic		19,400,673		16,168,115
Diluted[1]		21,394,822		16,828,115

See accompanying notes to the consolidated financial statements

[1] Outstanding stock options and performance warrants are the only instruments that are currently dilutive to earnings per share. All stock option and performance warrants have been included in the computation of diluted earnings per share.

Consolidated Statements of Cash Flows

For the year ended December 31,		2005		2004
Cash provided by (used in):				
Operating:				
Net earnings from continuing operations	$	9,625,417	$	2,877,740
Items not involving cash:				
Depletion, amortization and accretion		12,241,367		4,382,247
Future income taxes		5,284,877		826,669
Stock based compensation		1,941,169		559,481
Cash flow from continuing operations		29,092,830		8,646,137
Cash flow from discontinued operations (note 15)		206,968		---
		29,299,798		8,646,137
Change in non-cash operating working capital – continuing operations (note 14)		(405,860)		995,568
Change in non-cash operating working capital - discontinued operations (note 15)		(898,899)		---
Abandonments incurred during the year		(23,066)		(82,519)
		27,971,973		9,559,186
Investing:				
Exploration and development of properties		(42,637,391)		(13,001,81 1)
Acquisitions (note 3)		---		(4,884,696)
Dispositions (note 3)		296,000		---
Change in non-cash investing working capital - continuing operations (note 14)		3,672,368		1,186,158
Disposition of trust units – discontinued operations (note 15)		6,465,810		---
Disposition costs of oilfield service assets – discontinued operations (note 15)		(701,362)		---
		(32,904,575)		(16,700,34 8)
Financing:				
Issuance of common shares, net of share purchase loan		18,257,790		2,150,000
Share issue costs		(1,105,974)		---
Capital lease principal payments		(194,999)		---
Bank loan		(10,501,424)		7,018,226
Convertible debenture redemption – discontinued operations (note 15)		(3,000,000)		---
		3,455,393		9,168,226
Change in cash		(1,477,209)		2,027,065
Cash, beginning of year		2,027,065		---
Cash, end of year	$	549,856	$	2,027,065

See accompanying notes to the consolidated financial statements

Notes To Consolidated

Financial Statements

1. **Formation of Diamond Tree Energy Ltd.**

Diamond Tree Energy Ltd. (the "Company") was formed on December 31, 2004 as a result of the reverse takeover by Diamond Tree Resources Limited ("DTRL") of Wise Wood Corporation ("Wise Wood"). For accounting purposes, DTRL was deemed to have acquired Wise Wood and subsequent to the reverse takeover, Wise Wood changed its name to Diamond Tree Energy Ltd. DTRL was a private company incorporated in Alberta on April 9, 2001 and in the business of oil and gas exploration and development. Wise Wood was a TSX Venture Exchange listed public company in the oil field services business. In May 2005, the Company sold its remaining oil field service assets. Refer to Note 15 which shows the impact of discontinued operations in the consolidated financial statements of the Company as well as the initial December 31, 2004 fair values assigned to the Wise Wood net assets acquired.
Pursuant to a take over bid circular, Wise Wood acquired all of the issued and outstanding shares of DTRL in exchange for four common shares of Wise Wood for each common share of DTRL. The shares of the Company were then consolidated on a 10 for 1 basis. Effective December 31, 2004, DTRL was deemed to have acquired the 13,518,000 Wise Wood shares outstanding prior to the merger and share consolidation for approximately $2.4 million ($0.175 per share) plus $0.45 million of acquisition costs.
The consolidated financial statements of the Company for the year ended December 31, 2004 include the operating results of DTRL prior to the merger and the results of the merged company thereafter. All 2004 comparative figures are those of DTRL. Any disclosure of share, option or per share data in the financial statements reflects the post merger, post consolidation share structure.

2. **Significant Accounting Policies**

(a) Principles of consolidation:
The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Edenshaw Resources Ltd. and DTRL.

(b) Property and equipment and depletion and amortization:
The Company follows the full cost method of accounting for its petroleum and natural gas properties. All costs relating to the acquisition, exploration and development of petroleum and natural gas reserves, including asset retirement costs, are capitalized into cost centers. Such costs include land acquisition costs, geological and geophysical costs, lease rentals on undeveloped properties, costs of drilling of both productive and non-productive wells, related plant and production equipment costs and overhead costs which are directly attributable to acquisition, exploration and development activities. Dispositions of petroleum and natural gas properties are applied against capitalized costs, with gains or losses not ordinarily recognized unless such a sale would result in a greater than 20% change in the depletion and amortization rate.

Capitalized costs, excluding costs relating to unproved properties, are depleted and amortized using the unit-of-production method, based on estimated proved petroleum and natural gas reserves, before royalties, as determined by independent engineers. Petroleum and natural gas reserves are converted to a common unit of measure on the basis of six thousand cubic feet to one barrel of oil equivalent based on energy equivalency.

Costs of acquiring unproved properties are initially excluded from depletion calculations. These unproved properties are assessed periodically to ascertain whether impairment has occurred. When proved reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to costs subject to depletion calculations.

Oil and gas assets are evaluated in each reporting period to determine that their net book value is recoverable and does not exceed their fair value. The net book value is assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves and the lower of cost and market of unproved properties exceeds the net book value of the oil and gas assets. If the net book value of the oil and gas assets is assessed not to be recoverable, an impairment loss is recognized. The impairment loss is estimated as the amount by which the net book value of assets exceeds the sum of the fair value of proved and probable reserves and the cost (less any impairment) of unproved properties that have been subject to a separate test for impairment and contain no probable reserves. Fair value of proved and probable reserves is based on expected future net revenues (based on future product prices and costs) discounted at risk-free rates, without giving effect to abandonment, taxes or financing costs.
Other equipment is recorded at cost and amortized on a straight line basis at a rate of 20%.

(c) Inventory:
Inventory is recorded at the lower of average cost and estimated net realizable value. It consists of oilfield service inventory related to the Wise Wood acquisition and is included in current assets of discontinued operations.

(d) Interest in joint ventures:
The majority of the Company's petroleum and natural gas exploration activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

(e) Asset retirement obligation:
An asset retirement obligation ("ARO") associated with site restoration and abandonment of tangible long-lived assets is initially measured at fair value by estimating the cost a third party would incur in performing the tasks necessary to retire such assets. The fair value of the ARO is recorded in the financial statements as a liability, equal to the present value of expected future cash outflows, with a corresponding increase in the carrying amount of the related asset. Subsequent to initial measurement, the effect of the passage of time on the ARO, or accretion expense, and the amortization of the asset retirement cost are charged to earnings in the period. Subsequent changes in the estimated fair value of the ARO are capitalized and amortized over the remaining useful life of the underlying asset. Actual costs incurred upon the settlement of the ARO are charged against the ARO with the resulting difference recognized in income as a gain or loss.

(f) Flow-through shares
Expenditure deductions for income tax purposes related to exploratory and development activities funded by flow-through share arrangements are to be renounced to investors in accordance with income tax legislation. Share capital is reduced by the estimated cost of the renounced tax deductions when the expenditures are renounced.

(g) Measurement uncertainty:
Management is required to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. The amounts recorded for depletion and depreciation and the provision for asset retirement obligations are based on estimates. The ceiling test calculation is based on estimates of proved reserves, production rates, oil and natural gas prices, future costs and other relevant assumptions. By their nature these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in estimates in future periods could be significant. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which were fully tradable with no vesting restrictions. This option valuation model requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options and performance incentive warrants have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the calculated fair value, such value is subject to measurement uncertainty.

(h) Revenue recognition:
Revenue is recognized when the significant risks and rewards of ownership have transferred to the buyer, the seller's price to the buyer is fixed or determinable and there is reasonable assurance regarding collectibility of the consideration. Until all these criteria are met, it is not appropriate to recognize the transaction as a sale in the income statement and revenue would be deferred. Revenue associated with sales of natural gas, natural gas liquids and crude oil is recognized when the risks and rewards of ownership passes to the customer, generally with the passage of title.

(i) Financial instruments:
The Company carries a number of financial instruments, including cash, accounts receivable, bank indebtedness and accounts payable and accrued liabilities. Unless otherwise indicated, it is management's opinion that the Company is not exposed to significant credit risks arising from these financial instruments. The fair values of these financial instruments approximate their carrying values, unless otherwise noted.

The Company has no hedging contracts or fixed-price physical contracts in place at this time. For any derivative financial instruments used to hedge exposure to commodity price and foreign exchange fluctuations, the Company formally documents relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives used in hedge transactions are highly effective in offsetting changes in fair value or cash flows of hedged items. The Company does not use derivative financial instruments for trading purposes. Any gains or losses on financial instruments designated as hedges are deferred and are recognized in the period and in the same financial category in which the revenues or expenses associated with the hedged transactions are recognized. In the case where it is determined that the derivative financial instrument is no longer an effective hedge, gains or losses would be recognized in the period and the financial instrument would be "marked to market" for the remaining contract term.

(j) Income taxes:
The Company uses and liability method of accounting for income taxes. Under this method, the Company records future income taxes for the effect of any difference between the accounting and income tax basis of an asset or liability. Future income tax assets or liabilities are adjusted to reflect substantively enacted income tax rates and laws that will be in effect when the differences are expected to reverse.

(k) Per share amounts:
Earnings per share is computed based on the weighted average number of shares outstanding during the period. Diluted per share amounts are calculated giving effect to the potential dilution that would occur if options and performance incentive warrants to purchase common shares were exercised and other convertible instruments were converted. The Company uses the treasury stock method to determine the dilutive effect of stock options, performance incentive warrants and convertible debentures.

(l) Goodwill:
Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the fair value for accounting purposes of the net identifiable assets and liabilities of the acquired business. Goodwill is stated at cost less impairment and is not amortized. The goodwill balance is assessed for impairment annually at year-end or more frequently if events or changes in circumstances indicate that the asset may be impaired. The test for impairment is conducted by the comparison of the book value to the fair value of the entity. If the fair value is less than the book value, impairment is deemed to have occurred. The extent of the impairment is measured by allocation of the fair value of the entity to the identifiable assets and liabilities at their fair values. Any remainder of this allocation is the implied value of goodwill. Any excess of the book value of goodwill over this implied value is the impairment amount. Impairment is charged to earnings in the period in which it occurs.

(m) Stock based compensation:
The Company has a stock based compensation plan as described in Note 9. Stock based payments relating to stock options and performance warrants are measured using the fair value method of accounting. For stock options granted, fair value is measured at grant date and compensation expense is recognized in the financial statements over the vesting period of the awards with a corresponding increase in contributed surplus. For performance warrants, compensation expense is recognized over the life of the awards due to the contingent nature of their vesting. When the performance warrants vest, additional compensation expense is recognized to the extent of the fair value of the vested portion of the performance incentive warrants. Fair values are determined using the Black – Scholes option pricing model. Consideration received upon the exercise of stock options or performance warrants, together with the related amount of non-cash compensation cost recognized in contributed surplus, is recorded as an increase in share capital.

The Company also has in place a phantom stock option award program whereby certain employees, officers, directors or consultants may be granted phantom stock options ("PSO's") which entitle them to receive a cash payment, for each vested PSO, equal to the excess of the market price of the common shares at the time of exercise over the exercise price of the PSO. The Company recognizes an obligation and corresponding compensation expense for the PSO's which are in-the-money. Obligations are accrued on a graded vesting basis and represent the excess of the market value of the common shares over the exercise price of the PSO for the graded vested portion only. Obligations are recorded as a liability and revalued each reporting period based on the market value of the common shares and the number of graded vested PSO's outstanding at period end.

(n) Cash and cash equivalents:
Cash and cash equivalents consist of cash on hand and short term money market instruments with an original maturity of less than three months.

(o) Accounting for investments:
Investments in companies in which the Company does not control or exert significant influence over are accounted for using the cost method of accounting. The investment is initially recorded at cost and earnings are recognized only to the extent they are received or receivable. Any loss in value of the investment that is other than a temporary decline would result in recognition of the loss. If the investment is written down, any loss in value would not be reversed if there was a subsequent increase in value unless the investment was sold and the gain realized.

(p) Transportation costs:
The Company records revenue before transportation charges and transportation charges are included as an operating expense on the consolidated statement of income.

3. Acquisitions and Dispositions

Acquisition of Edenshaw Resources Ltd.

On November 17, 2004, DTRL acquired all outstanding shares of Edenshaw Resources Ltd. ("Edenshaw"), a private oil and gas company, for aggregate cash consideration of $5.6 million. The acquisition has been accounted for as a purchase as follows:

Allocation of purchase price:			
Edenshaw net assets acquired and liabilities assumed			
Current assets	$		864,142
Current liabilities – income taxes payable			(91,459)
Asset retirement obligations			(10,000)
Petroleum and natural gas properties		7,240,000	
Goodwill		246,515	
Future income taxes		(2,601,819)	
			4,884,696
	$		5,647,379

Cash consideration comprised of:		
Net assets and liabilities assumed	$	5,211,412
Transaction costs		435,967
	$	5,647,379

Property Disposition

Effective June 30, 2005 and closing September 30, 2005, the Company sold its heavy oil interests in Saskatchewan to a private company for cash proceeds, net of adjustments, of $296,000.

4. Property and Equipment

		2005		2004
Petroleum and natural gas properties	$	81,712,293	$	39,425,059
Equipment under capital lease		1,176,668		—
Asset retirement cost		2,301,758		942,318
Other		96,544		42,388
		85,287,263		40,409,765
Accumulated depletion and amortization		(18,793,348)		(6,653,345)
	$	66,493,915	$	33,756,420

During the year ended December 31, 2005, $695,000 (2004 - $711,000) of general and administrative costs related to exploration and development activity were capitalized.

The net book value of equipment under capital lease is $972,087 (2004 – nil).
At December 31, 2005, the depletion calculation excluded unproved properties of $9,448,000 (2004 - $3,184,000) and salvage values of $1,639,000 (2004 – $617,000). Future development costs of proved undeveloped reserves of $3,790,000 (2004 - $3,358,000) were included in the depletion and amortization calculations.

The Company performed a ceiling test calculation at December 31, 2005 to assess the recoverable value of its oil and gas properties. The oil and gas future prices are based on the commodity price forecast of the Company's independent reserve evaluators. These prices have been adjusted for heating content, quality and transportation parameters specific to the Company. The following table summarizes the benchmark prices used in the ceiling test calculation.

Year	WTI Oil ($U.S./bbl)	AECO Gas ($Cdn/mcf)	Foreign Exchange Rate
2006	60.00	11.50	0.85
2007	61.20	10.50	0.85
2008	62.45	8.90	0.85
2009	61.60	8.50	0.85
2010	59.55	8.70	0.85
2011	55.15	8.90	0.85
	Escalate thereafter 2.0% year		0.85

The undiscounted value of future net revenues from the Company's proved reserves exceeded the carrying value of the oil and gas properties at December 31, 2005.

5. **Bank Loans**

At December 31, 2005 DTRL had available a $24.0 million (2004 - $10.6 million) revolving operating loan facility with a Canadian chartered bank. At December 31, 2005 drawings against this loan were $nil (2004 - $10.5 million) and the Company held cash of $450,000 (2004 – $2.0 million). The loan bears interest at the bank's prime rate plus 0.25% and the next annual review date has been scheduled for April 30, 2006. Security for this facility is by way of a general security agreement providing a security interest over all present and after acquired personal property and a floating charge on all lands. At December 31, 2005 there were no covenant violations.

6. **Capital Lease**

On March 23, 2005, the Company entered into a lease obligation for field compression facilities that is being treated as a capital lease for accounting purposes. The interest rate implicit in the lease is 7.55% per annum, the monthly lease instalment is $27,687, the security for the lease is the equipment itself and the term of the lease is three years, with an April 2008 expiry. The Company is required to make the following annual principal repayments:

		Annual principal repayments
2006	$	267,248
2007		288,139
2008		426,282
Total		981,669
Less current portion		(267,248)
Long term capital lease portion	$	714,421

7. **Asset Retirement Obligation**

Total future asset retirement obligations were estimated by management based on the Company's working interest in its wells and facilities, estimated costs to remediate, reclaim and abandon the wells and facilities, before deduction of salvage values, and the estimated timing of the costs to be incurred in future periods. The Company has estimated the net present value of its total asset retirement obligations to be approximately $2.5 million at December 31, 2005 (December 31, 2004 - $1.0 million), based on a total future liability of $6.5 million (December 31, 2004 - $1.7 million). It is expected that $2.6 million of the total future liability will be incurred before 2016 and the remaining $3.9 million by 2033. The Company used a credit adjusted risk-free rate of 9% (December 31, 2004 – 9%) and an inflation rate of 2% (December 31, 2004 – 2%) to calculate the present value of the asset retirement obligation. The following table reconciles change in the Company's total asset retirement obligation:

Year ended December 31,		2005		2004
ARO, beginning of year	$	956,059	$	511,076
Increase in liabilities		1,393,441		467,913
Settlement of liabilities		(23,066)		(82,519)
Acquisition of liabilities		---		10,000
Disposition of liabilities		(34,000)		---
Accretion expense		101,363		49,589
ARO, end of year	$	2,393,797	$	956,059

8. **Income Taxes**

The provision for income taxes in the consolidated financial statements differs from the result which would have been obtained by applying the combined federal and provincial tax rate of 37.62% (2004 – 39%) to the Company's earnings before income taxes. The difference results from the following items:

Year ended December 31,		2005		2004
Expected income taxes on earnings before income taxes	$	5,676,273	$	1,446,269
Difference between resource allowance and non-deductible resource items		(215,289)		(133,057)
Alberta Royalty Credits		(117,538)		(137,355)
Reduction in enacted rates		(688,291)		(493,331)
Capital taxes		33,959		---
Other non taxable items		---		(66,707)
Non-deductible expenses, including stock based compensation		773,913		214,821
	$	5,463,027	$	830,640

Current taxes of $178,150 for the year ended December 31, 2005 are comprised of income tax of $144,191 (2004 - $ nil) and corporation capital taxes of $33,959 (2004 - $3,971).

The components of the net future income tax liability are as follows:

December 31,		2005		2004
Future income tax assets:				
Attributed crown royalty income benefit	$	101,202	$	73,285
Share issue costs		315,158		---
Asset retirement obligations		830,648		350,874
		1,247,008		424,159
Future income tax liabilities:				
Carrying value of property and equipment in excess of tax basis		12,747,008		7,024,159
Net future income tax liability	$	11,500,000	$	6,600,000

At December 31, 2005, subject to confirmation by income tax authorities, the following tax pools are available for deductions against future income from oil and gas related exploration and development activities:

Canadian oil and gas property expenses	$	9,400,000
Canadian development expenses		10,400,000
Canadian exploration expenses		66,000
Undepreciated capital cost		10,900,000
Share issue costs		885,000

9. **Share Capital**

(a) Authorized:

Unlimited number of common voting shares.
Unlimited number of preferred shares issuable in series, with rights and privileges to be determined upon issuance.

(b) Common shares issued:

	2005		2004	
	Number of Shares	Amount $	Number of Shares	Amount $
Balance beginning of year	18,711,798	$14,545,470	40,300,000	$9,379,820
Issued for cash upon exercise of DTRL options			600,000	300,000
			40,900,000	9,679,820
Shares issued to DTRL shareholders on a 4 for 1 basis			163,600,000	---
Shares held by Wise Wood shareholders			13,518,000	2,365,650
Share consolidation on a 10 for 1 basis			(159,406,202)	
			17,711,798	$12,045,470
Issued for cash upon exercise of options	274,000	357,500		
Issued for cash upon private placement	3,509,400(2)	17,900,290(2)	1,000,000(1)	2,500,000(1)
Share issue costs		(1,105,974)		
Future tax benefit of share issue costs @ 34.8%		384,877		
Contributed surplus drawdown re: option exercises		9,544		
Balance end of year	22,495,198	$32,091,707	18,711,798	$14,545,470

[(1)] On December 31, 2004 the Company closed a private placement of units with each unit consisting of one common share and 2.5 common share performance warrants, for the subscription price of $2.50 per unit. Refer to Note 10 for information on the share purchase loans that the Company provided for a portion of the subscription proceeds. Directors, officers and employees of the Company purchased all of the units of this private placement.
[(2)] On September 29, 2005, the Company closed a private placement resulting in the issuance of 3.5 million common shares at $5.10 per share of which 22,000 shares were issued to directors, officers and employees. On November 10, 2005, the Company closed a private placement to an employee resulting in the issuance of 9,400 common shares at $5.35 per share. The transactions were consummated at fair value.

(c) Stock options:
The Company has a stock option program whereby directors, officers, employees and consultants are eligible to receive options. Exercise prices range from $1.25 to $6.00 per share and expiry dates range to November 16, 2010. For options granted during 2004 and 2005 and future option grants, one third of the options vest at the time of grant, one third on the first anniversary and the remaining options vest on the second anniversary.

	2005		2004	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding, beginning of year	1,940,000	$2.20	700,000	$1.25
Granted	625,000	5.73	1,405,000	2.50
Exercised	(274,000)	1.30	(240,000)	1.25
Cancelled or expired	(5,000)	5.00	---	---
Wise Wood options exchanged [(1)]			75,000	2.40
Options outstanding, end of year	2,286,000	$3.26	1,940,000	$2.20
Exercisable at year end	1,400,986	$2.79	1,003,328	$1.92
Weighted average remaining contractual life	3.9 years		4.1 years	

(1) As a result of the DTRL-Wise Wood business combination, every ten outstanding Wise Wood options were exchanged for one option of the Company.

For the year ended December 31, 2005, compensation expense of $1,015,649 (December 31, 2004 - $473,712) has been recorded for the stock options. The assumptions used in the computation of the fair values of the stock options granted during 2005 are as follows:

Weighted average fair value per option granted	$1.99
Weighted average expected volatility	62%
Risk free interest rate	3.7%
Expected life (years)	2.0

(d) Performance Warrants:
In conjunction with the December 31, 2004 private placement of units referred to in Note 9(b), 2.5 million performance warrants were issued, with private placement subscribers receiving 2.5 performance warrants for each common share purchased.

Each performance warrant entitles the holder to acquire one share of the Company for a price of $2.50 per share (being the ascribed value of a Wise Wood share, adjusted for the ten-for-one share consolidation, in the DTRL-Wise Wood business combination). The performance warrants expire after a seven year term and are exercisable by a holder only during the period that the holder is a director, employee or consultant of the Company. Should a holder cease to be a director of the Company, or should such holder's employment or consulting services terminate prior to exercise of the performance warrants, the expiry date will be accelerated and all of the said holder's performance warrants will terminate. Certain provisions exist which permit acceleration of the vesting of the performance warrants upon a change of control of the Company.

The performance warrants may be exercised only to the extent that they: (1) have vested and (2) are exercisable. No performance warrants shall vest prior to one year following the date of grant. Performance warrants are exercisable at any time during their term, in the following percentages, upon Company shares reaching the following 20-day weighted average trading prices:

Percentage exercisable	Weighted average trading price of common shares	Performance warrant exercise price
33 1/3%	$3.50	$ 2.50
33 1/3%	$4.50	$ 2.50
33 1/3%	$5.50	$ 2.50

All 2.5 million performance warrants are fully vested and exercisable. For the year ended December 31, 2005, compensation expense of $886,533 (December 31, 2004 - $ nil) has been recorded for the performance warrants.

The assumptions used in the computation of the fair value for the performance warrants, based on the grant being made at market price on December 31, 2004, are as follows:

Fair value per warrant granted	$0.74
Expected volatility	49%
Risk free interest rate	3.0%
Expected life (years)	2.0

(e) Phantom Stock Options:

During the fourth quarter of 2005, the Company implemented a phantom stock option award program. Under this program, employees, officers, directors or consultants may receive PSO's which entitle them to a cash payment, for each vested PSO, equal to the excess of the market price of the common shares at the time of exercise over the exercise price of the option. The PSO's expire after a five year term. They are exercisable by a holder only during the period that the holder is an employee, officer, director or consultant of the Company. Certain provisions exist for: (i) the acceleration of expiry dates upon termination or ceasing to be an employee, officer, director or consultant of the Company and (ii) the acceleration of vesting upon change of control of the Company. PSO's vest on a graded basis over three years. They become vested and exercisable only to the extent that they meet both time and performance criteria. To meet the performance criteria, common shares of the Company must achieve certain 20 day volume weighted average closing trading prices.

For PSO's outstanding at the end of 2005, the trading prices required to meet the performance criteria range from $5.50 to $8.35. The following table summarizes the information about the outstanding PSO's:

	2005	
	Number of PSO's	Weighted average exercise price
PSO's outstanding, beginning of year	---	$0.00
Granted	130,000	4.83
Exercised	---	0.00
Forfeited	---	0.00
PSO's outstanding, end of year	130,000	$4.83
Exercisable at year end	---	$0.00
Weighted average remaining contractual life	4.7 years	

During the year, the Company accrued stock based compensation expense of $79,000 (2004 - nil) relating to the PSO's.

10. Share Purchase Loan

In conjunction with the December 31, 2004 private placement of units referred to in Note 9(b), the Company provided non-interest bearing share purchase loans in the amount of $650,000 to certain employees of the Company. As security for the share purchase loans, the shareholders have collectively assigned 260,000 units, representing the common shares, performance warrants and any shares exercisable upon conversion of the performance warrants, to the Company. The market value of the shares held as collateral for the loans, based on the current trading price as at March 3, 2006 is approximately $1.7 million. The share purchase loans have a mandatory repayment date the earlier of (i) January 1, 2008 or (ii) two business days after receipt of any proceeds from the sale of the related securities. Since the share purchase loans do not meet the criteria for recognition of an asset, they are recorded as a reduction of shareholders' equity and afforded stock option treatment in accordance with the Company's stated policy for stock-based compensation. For the year ended December 31, 2005, related compensation expense of $38,987 (December 31, 2004 - $85,769) has been recorded.

The assumptions used in the computation of the fair values of the share purchase loan are as follows:

	Stock options
Fair value per option pledged	$0.54
Expected volatility	34%
Risk free interest rate	3.0%
Expected life (years)	2.0

11. Contributed Surplus

The following schedule shows the continuity of contributed surplus:

		2005		2004
Balance, beginning of year	$	559,481	$	---
Provision of share purchase loans		38,987		85,769
Grant of stock options		1,015,649		473,712
Grant of performance warrants		886,533		---
Exercise of stock options		(9,544)		---
Balance, end of year	$	2,491,106	$	559,481

12. Commitments and Contingencies

The Company is committed to lease office premises with future annual lease payments, as follows:
2006: $235,700, 2007: $165,000. The office lease expires on May 31, 2007.

The Company enters into equipment rental agreements with certain equipment manufacturers on an as required basis. The Company is usually committed to a minimum rental period of three months. The minimum guaranteed rental payments at December 31, 2005 are approximately $17,550 (December 31, 2004 - $36,000).

On December 12, 2005, the Company announced the signing of a farm-in agreement with a four well commitment. On February 3, 2006, the Company entered into an agreement to acquire additional seismic data over the farm-in area. Estimated committed drilling and seismic costs relating to this farm-in over the next twelve months total $4.5 million.

13. Financial Instruments

As disclosed in Note 2(i), the Company holds various forms of financial instruments. The nature of these instruments and the Company's operations expose the Company to interest rate risk, foreign exchange risk, fair value risk and industry credit risk. The Company manages its exposure to these risks by operating in a manner that minimizes its exposure to the extent practical.

(a) Fair value of financial assets and liabilities: The carrying value of accounts receivable, prepaid expenses and accounts payable and accrued liabilities approximate their fair value due to their relatively short periods to maturity. Any bank loan balance approximates its fair value since it bears interest at a floating rate.

(b) Credit risk: Substantially all of the accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks. At December 31, 2005 82% (2004 – 74%) of the Company's receivables were from one customer.

(c) Interest rate risk: The Company is exposed to fluctuations in interest rates. At December 31, 2005, the Company has $ nil (December 31, 2004 - $11.2 million) of debt with a variable rate of interest.

(d) Foreign exchange risk: The Company is exposed to foreign currency fluctuations as crude oil and natural gas prices received are referenced to U.S. dollar denominated prices.

14. Supplemental Cash Flow Disclosure

		2005		2004
Accounts receivable	$	(4,310,684)	$	(1,329,884)
Inventory		---		(283,779)
Share of amount due from joint venture		---		(201,274)
Prepaid expenses		5,389		(297,296)
Income taxes payable		62,241		75,439
Notes payable		---		469,599
Accounts payable and accrued liabilities		7,509,562		3,552,487
	$	3,266,508	$	1,985,292

Change in non-cash working capital from continuing operations				
Operating	$	(405,860)	$	995,568
Investing		3,672,368		1,186,158
Acquired in exchange for shares (Note 1)		---		(196,434)
	$	3,266,508	$	1,985,292

Continuing operations		2005		2004
Cash interest paid	$	509,934	$	244,513
Cash taxes paid	$	115,909	$	16,020

15. Discontinued Operations

Pursuant to the December 31, 2004 acquisition of Wise Wood by DTRL, the merged company, Diamond Tree Energy Ltd., adopted a plan to divest of the oil field services assets formerly held by Wise Wood. Such operations have been included in the balance sheet as assets and liabilities of discontinued operations and in the income statement as earnings or loss from discontinued operations.

On May 2, 2005 the Company sold its remaining oil field service assets to Eveready Income Fund, a publicly traded entity, for total proceeds of $4,650,000. Proceeds included 1.2 million trust units of Eveready Income Fund, then valued at the weighted average trading price of $3.75 per unit. The units did not become freely tradable until September 4, 2005.

On June 14, 2005, the Company sold, by way of a purchase and sale agreement, the 1.2 million trust units of Eveready Income Fund to an arm's length purchaser for $5.00 per unit (subject to adjustments to the selling price as described below). At closing, the Company received a $3.6 million deposit from the purchaser, representing 60% of the sale price. The deposit was initially recorded as deferred proceeds on the balance sheet and the trust units remained on the balance sheet at their purchased value of $3.75 per unit.
By December 19, 2005 the purchaser had resold all 1.2 million trust units. The proceeds to the Company were then determinable which allowed for the removal of the deferred proceeds and trust units from the balance sheet and a net gain to be recognized in the income statement. Pursuant to the purchase and sale agreement, the Company's selling price was adjusted for the proceeds ultimately realized by the purchaser. Since the proceeds ultimately realized by the purchaser of the trust units exceeded $5.00 per unit, 50% of the excess was a positive adjustment to the selling price. The Company realized a before tax gain of $1,965,810 on the sale of the trust units.

The following table presents the impact of discontinued operations in the Consolidated Statements of Income and Retained Earnings:

		For the twelve months ended, Dec 31, 2005	For the twelve months ended, Dec 31, 2004
Revenue	$	1,867,705	---
Expenses(1)		1,660,737	---
Income before income taxes		206,968	---
Income taxes		(74,500)	---
Loss on disposal of oilfield service assets, net of tax recovery of $428,000		(2,118,666)	---
Gain on disposal of trust units, net of tax of $354,000		1,611,810	
Loss from discontinued operations	$	(374,388)	---

(1) No depreciation and amortization was recorded as the assets were held for sale

The following table presents the impact of discontinued operations in the Consolidated Balance Sheets:

		As at Dec 31, 2005	As at Dec 31, 2004
Assets	$		
Accounts receivable		422,947	682,373
Inventory		---	283,779
Prepaid expenses		---	187,057
Oilfield service assets		---	---
Total current assets		422,947	1,153,209
Non-current assets - oilfield service assets		---	6,345,805
Total Assets	$	422,947	7,499,014
Liabilities			
Accounts payable and accrued liabilities		---	487,176
Bank loans		---	672,386
Notes payable		---	469,599
Total current liabilities		---	1,629,161
Non-current liabilities - convertible debentures		---	3,000,000
Total Liabilities	$	---	4,629,161
Net Assets of discontinued operations	$	422,947	2,869,853
Non-cash operating working capital of discontinued operations	$	422,947	(475,952)
Change in non-cash operating working capital	$	898,899	

The $422,947 accounts receivable at December 31, 2005 relates to a holdback for post-closing adjustments from the sale of the oilfield service assets. It was collected subsequent to year end. Refer to Note 17.

During 2005, Wise Wood's bank loan, U.S. dollar denominated notes payable and secured, convertible debentures were paid in full using the proceeds from divesting of the oilfield service assets.

16. Comparative Figures

Certain figures have been reclassified to conform to the current year's presentation.

17. Events Subsequent to December 31, 2005

(a) Subsequent to December 31, 2005, 113,000 options were exercised for total cash proceeds to the Company of $207,500.

(b) As settlement for the holdback receivable relating to the May 2, 2005 sale of its oilfield service assets, the Company received 54,176 units of Eveready Income Fund on January 27, 2006. These units were recorded at their weighted average trading price of $7.81 per unit. Based on their weighted average trading price as at March 3, 2006, the market value of the units is approximately $6.55 per unit.

CORPORATE INFORMATION

OFFICERS

Don D. Copeland (P.Eng.)
Chairman and CEO

Kelly J. Ogle
President

David A. Cheesman (B.Sc. Geol.)
VP Exploration

David Keenan (P. Eng.)
VP Engineering

Kelly A. Tomyn (CA)
VP Finance and CFO

Nicholas P. Fader
Corporate Secretary

DIRECTORS

Don D. Copeland (P.Eng.)
Chairman & CEO Diamond Tree

Kelly J. Ogle
President of Diamond Tree

Thomas M. Alford
President & CEO of IROC Systems Corporation

Charles W. Berard (P. Eng., LLL, LLB)
Partner Macleod Dixon Law firm

Howard W. Dixon (B. Comm.)
Independent businessman

Fred A. Moore
President of NUSCO Supply and Manufacturing

Gary B. Unrau (B. Sc.)
Independent businessman and geologist

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BANKERS
ATB Financial, Calgary, AB

EVALUATION ENGINEERS
AJM Petroleum Consultants, Calgary, AB

LEGAL COUNSEL
Bennett Jones LLP, Calgary, AB
Macleod Dixon LLP, Calgary, AB

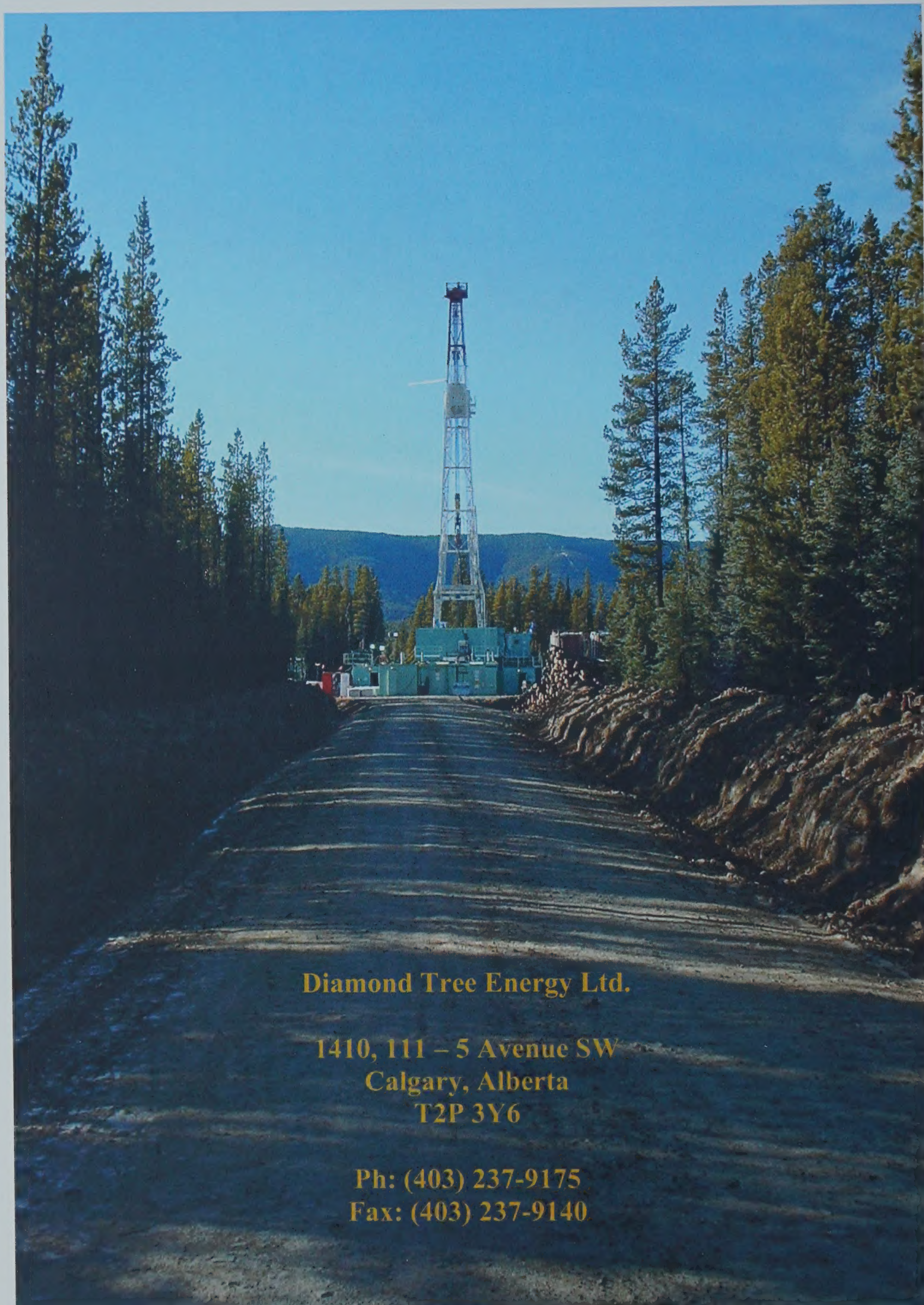
REGISTRAR AND TRANSFER AGENT
CIBC Mellon Trust Company, Calgary, AB

TORONTO STOCK EXCHANGE
Trading Symbol: DT

ABBREVIATIONS

CDN$	Canadian dollar
US$	United States dollar
ARTC	Alberta Royalty Tax Credit
bcf	Billions of cubic feet
boe	Barrels of oil equivalent
boe/d	Barrels of oil equivalent per day
bbl	Barrels of oil or natural gas liquids
bbl/d	Barrels of oil per day
GJ	Gigajoule
mbbls	Thousands of barrels
mboe	Thousands of barrels of oil equivalent
mmboe	Millions of barrels of oil equivalent
mmbtu	Millions of British Thermal Units
mcf	Thousands of cubic feet
mmcf	Millions of cubic feet
mmcf/d	Millions of cubic feet per day
mstb	Thousands of stock-tank barrels
NGL	Natural gas liquids
WTI	West Texas Intermediate

Diamond Tree's Annual General Meeting will be held on Wednesday, May 17, 2006 at 2:00 p.m. in the Viking Room of the Calgary Petroleum Club.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